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# In the Supreme Court
OF THE
# United States

OCTOBER TERM, 1931

## No. 528

PEIRCE COOMBES,
*Petitioner,*

vs.

MILTON E. GETZ,
*Respondent.*

## BRIEF FOR RESPONDENT.

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## BRIEF FOR RESPONDENT

**In opposition to petition for writ of certiorari to the Supreme Court of the State of California—82 Cal. Dec.* 103, 1 P. (2d) 992, R. p. 37 (July 23, 1931); rehearing denied 82 Cal. Dec. 557, 4 P. (2d) 157, R. p. 51 (August 21, 1931).**

### PRELIMINARY STATEMENT.

From its adoption in 1879 until November 4, 1930, the Constitution of the State of California contained the following provision (which was self-executing—*Winchester v.*

*The reference is to "California Decisions," the unofficial advance publication of the opinions of the appellate courts of California. The case has not yet appeared in the official California reports.

*Howard*, 136 Cal. 432, 439-441, 64 Pac. 692, 69 Pac. 77) imposing liability, regardless of fault, upon directors of corporations (Art. XII, Sec. 3):

> "The directors or trustees of corporations and joint-stock associations shall be jointly and severally liable to the creditors and stockholders for all moneys embezzled or misappropriated by the officers of such corporation or joint-stock association during the term of office of such director or trustee."

From its adoption the Constitution at all times contained also the following express reservation of the right to amend and repeal all laws relative to corporations (Art. XII, Sec. 1):

> "All laws now in force in the State concerning corporations, and all laws that may be hereafter passed pursuant to this section, may be altered from time to time or repealed."

On November 4, 1930, the constitutional provision imposing the directors' liability was repealed without a saving clause (Senate Const. Amdt. No. 24, Cal. Stats. 1929, pp. 2238-2239, ratified at election of November 4, 1930; see certificate of Secretary of State, R. p. 37).

In the case at bar the Supreme Court of California decided that, in view of the reserved power of repeal, above quoted, and since the liability imposed upon directors by the constitutional provision was unknown at common law, the repeal of that provision without a saving clause, extinguished all rights of action under it, including all pending cases which had not been reduced to final judgment (R. pp. 37, 51). On this ground the court dismissed an appeal which the petitioner had theretofore

taken to it in this case. The circumstances leading up to this ruling were briefly as follows:

The plaintiff is assignee of a claim for $617.50 against Getz Bros. & Company, a California corporation (R. p. 1). He brought this suit on behalf of himself and other creditors (R. p. 19), to recover from the directors of Getz Bros. & Company sums in excess of $550,000, which he alleged had been embezzled by an officer of the corporation. The method of the alleged embezzlement is set forth in the complaint (paras. VII-VIII, R. pp. 2-11), but is immaterial on this application, because it is admitted that Milton E. Getz, the sole respondent, had no connection with the embezzlement, and that the only basis for the assertion of any liability against him is the repealed constitutional provision (see R. pp. 12-13).

The trial court sustained a demurrer to the complaint on the ground that the alleged cause of action was barred by the statute of limitations (R. pp. 27-30). The plaintiff declined to amend and took an appeal to the State Supreme Court. While the appeal was pending, the constitutional provision was repealed, as above stated (R. p. 37). On the basis of this repeal the respondent Getz made a motion to dismiss the appeal which the court granted (R. p. 37; 82 Cal. Dec. 103, 1 P. (2d) 992). A petition for rehearing was denied (R. pp. 50, 51; 82 Cal. Dec. 557, 4 P. (2d) 157).

The present application is to have this court review the order dismissing the appeal. The application is on the ground that this order gave the repeal of the provision for directors' liability an effect violating the impairment of contract clause of the Federal Constitution. No claim is

put forward by the petitioner under the Fourteenth Amendment.

We submit that the ruling of the state court was sound and right and in no way contrary to the Constitution of the United States.

## ARGUMENT.

### I.

**Where a right of action did not exist at common law, but depends solely upon a statutory or constitutional provision, the repeal of such provision without a saving clause extinguishes all rights under it which have not been reduced to final judgment.**

The principle stated in the heading is a familiar one, and the application of it by the state court in the case at bar is well supported by its own prior decisions and by the decisions of this court.

In *Flanigan v. Sierra County*, 196 U. S. 553, a case which involved the repeal of a California statute imposing licenses, this court stated the general principle as follows (p. 560):

> "The general rule is that powers derived wholly from a statute are extinguished by its repeal. Sutherland on Statutory Construction, sec. 165. And it follows that no proceedings can be pursued under the repealed statute, though begun before the repeal, unless such proceedings be authorized under a special clause in the repealing act."

To the same effect are:

*The Assessors v. Osbornes*, 9 Wall. 567, 575;

*Moss v. Smith*, 171 Cal. 777, 787-789, 155 Pac. 90, 94 (Repeal of statute imposing liability upon di-

rectors for creating debts in excess of subscribed capital stock);

*Willcox v. Edwards,* 162 Cal. 455, 123 Pac. 276 (Applying principle to repeal of state constitutional provision which had authorized recovery of money paid in purchase of corporate stocks on margin);

*Krause v. Rarity,* 210 Cal. 644, 293 Pac. 62;

*People v. Bank of San Luis Obispo,* 159 Cal. 65, 112 Pac. 866;

*Napa State Hospital v. Flaherty,* 134 Cal. 315, 66 Pac. 322.

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II.

**The application of the foregoing principle to the repeal of Section 3 of Article XII of the Constitution of the State of California, providing for directors' liability, did not violate the impairment of contract clause of the Federal Constitution, for the reason that the right of amendment and repeal was at all times specifically reserved by Section 1 of Article XII of the State Constitution.**

We do not dispute that, under the decisions of the Supreme Court of California, the liability of the directors of a corporation under the constitutional provision in question was "contractual." Though imposed alike upon guilty and innocent directors, it was, under the decisions of the state courts, a liability resembling suretyship; the directors being sureties against embezzlements or misappropriations by corporate officers, and the creditors' claim against the directors being measured by the loss which the embezzlement or misappropriation had caused the corporation (*Dean v. Shingle,* 198 Cal. 652, 246 Pac. 1049).

The same article, however, of the State Constitution, which imposes the liability upon which this suit is brought, contains the specific reservation (quoted supra) of the right to amend and repeal the laws concerning corporations. When, therefore, the plaintiff's assignor extended credit to Getz Bros. & Company, and so entered into the "contract" for the directors' liability here asserted, such credit was extended with full knowledge that the liability might at any time be altered or repealed. The fact that the liability could be repealed was as much a part of the "contract" as the liability itself. This court has many times pointed out that the reserved power of amendment and repeal necessarily enters into "contracts" of this kind.

In *Sherman v. Smith*, 66 U. S. 587, the statute, organizing a bank in which Sherman became a stockholder, provided that the stockholders should not be subject to any individual liability for the bank's debts. The statute reserved the right of amendment and repeal, and on that ground this court sustained, against attack based on the contract clause, a subsequent statute imposing a stockholder's liability (see pp. 587-588). The court said (pp. 592, 593):

> "The argument on the part of the plaintiff is, that this stipulation of the stockholders in the articles of association from [*sic*] exemption from all personal liability for the debts of the institution, constitutes a contract within the authority of the act under which it was organized, that cannot be legally impaired by the provision in the constitution of New York, or by the act of 1849, which seeks to change the obligation, and impose upon them personal liability; that, in respect to this bank, the provision in the constitution

and the law are void as against the Constitution of the United States.

* * * * * * *

Now, the 32nd section, which reserved to the Legislature the power to alter or repeal the act, by necessary construction, *reserved the power to alter or repeal all or any one of these terms and conditions, or rules of liability, prescribed in the act. The articles of association are dependent upon, and become a part of, the law under which the bank was organized, and subject to alteration or repeal the same as any other part of the general system''* (italics ours).

In *Looker v. Maynard,* 179 U. S. 46, this court, in sustaining a Michigan statute permitting cumulative voting, pointed out the application to corporation laws in general of the reserved right of amendment and repeal. The court, after quoting with approval the case of *Sherman v. Smith,* just cited, said (pp. 53-54):

"The case of *Miller v. State,* 15 Wall. 478, was this: * * * In the same year [1850] a railroad corporation was organized under that act for the construction of a railroad from the city of Rochester to the town of Portage; and in 1851, by a statute amending the charter of the city of Rochester, that city was authorized to become a stockholder in the corporation, and to appoint four of the thirteen directors. Stat. 1851, c. 389, sec. 24. In 1867, the legislature passed another statute, authorizing the city to appoint seven of the thirteen directors. Stat. 1867, c. 59. This court upheld the validity of the latter statute, upon the ground that the reservation in the constitution of 1846, and in the statutes of 1828 and 1850, of the power to alter or repeal the charter, clearly authorized the legislature to augment or diminish

the number or to change the apportionment, of the directors as the ends of justice or the best interests of all concerned might require. 15 Wall. 492, 498. *The full extent and effect of the decision are clearly brought out by the opinion of two justices who dissented for the very reason that the agreement with respect to the number of directors which the city should elect was not a part of the charter of the company, but was an agreement between third parties, outside of and collateral to the charter, and which the legislature could not reserve the power to alter or repeal. 15 Wall. 499. That case cannot be distinguished in principle from the case at bar''* (italics ours).

The petitioner quotes (Pet. p. 25) a passage from the opinion in *Greenwood v. Freight Co.*, 105 U. S. 13, but does not quote the following passage from the same opinion, which has a much more direct bearing on the case at bar (p. 21):

> "This history of the reservation clause in acts of incorporation supports our proposition, that whatever right, franchise, or power in the corporation depends for its existence upon the granting clauses of the charter, is lost by its repeal."

We call attention also to the following cases:

*Citizens Savings Bank v. Owensboro*, 173 U. S. 636, 644 (" * * * the reserved power deprives the contract of its irrevocable character and submits it to legislative control. The foundation of this rule is that a general statute reserving the power to repeal, alter or amend is by implication read into a subsequent charter and prevents it from becoming irrevocable");

*Polk v. Mutual Reserve Life Fund,* 207 U. S. 310, 325-326 (Sustaining statutory amendment authorizing company to change from assessment life insurance business to life insurance business of every kind);

*Hammond Packing Co. v. Arkansas,* 212 U. S. 322, 346 ("The claim of an irrepealable contract cannot be predicated upon a contract which is repealable");

*Missouri Pacific Ry. Co. v. Kansas,* 216 U. S. 262, 274-275 ("* * * the proposition amounts simply to saying that an irrepealable contract arose from a contract which was repealable. * * * And, of course, this reason is controlling, irrespective of the scope of the alleged charter right, since whatever be the extent of the right conferred it was subject to the reserved power");

*Calder v. Michigan,* 218 U. S. 591, 599 (*Quo warranto* to enforce statute, passed under reserved power, repealing charter. Defendants set up bondholders' rights. "They contracted subject not paramount to the proviso for repeal * * *").

The doctrine invoked in support of the petition for certiorari is, of course, the familiar doctrine of the Dartmouth College case (*Trustees of Dartmouth College v. Woodward,* 4 Wheat. 518). But in invoking this doctrine, the petitioner ignores the equally familiar qualification of that doctrine which exists where the power of amendment or repeal is reserved. The principle is not limited to charters, but applies, as is shown by the cases already cited, to many situations arising under the corporation laws.

It should be noted in the application of these principles that the language of the California Constitution con-

tains "the broadest possible statement of the reserved power" (*Melaven v. Schmidt,* 34 N. M. 443, 283 Pac. 900, 901, involving constitutional provision in identical language). The reserved power in some states is limited. In California, however, "all laws * * * concerning corporations * * * may be altered from time to time or repealed" (Cal. Const. Art. XII, Sec. 1).

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## III.

**Comment upon petitioner's arguments and authorities.**

We have examined all the authorities cited in the petition. No one of them involves directors' liability, and only four have to do with the alteration or repeal of statutes imposing stockholders' liability. These four are:

*Bernheimer v. Converse,* 206 U. S. 516 (Pet. pp. 6, 24);

*Hawthorne v. Calef,* 2 Wall. 10 (Pet. pp. 6, 7, 8, 20);

*Irvine v. Elliott* (D. C. Del.), 203 Fed. 82 (Pet. pp. 7, 21);

*Ochiltree v. Railroad Co.,* 21 Wall. 249 (Pet. pp. 7, 20).

No one of these cases is in point because no one of them involves or contains any discussion of the reserved power of amendment or repeal.

The petitioner argues that the reserved power applies only to laws affecting the relationship of corporations or their stockholders to one another or to the state, and cannot "affect * * * contracts between directors and creditors only" (Pet. pp. 8-9). The fallacy in this argu-

ment is, we submit, obvious. It is true that the constitutional liability of directors in California was "contractual," but it was at the same time a liability created by law and, as we have shown, the reserved right of repeal was a part of the "contract" between the respondent and the assignor of petitioner, just as much as the liability itself. Such decisions of this court as *Sherman v. Smith*, *Looker v. Maynard* and *Calder v. Michigan* (quoted supra) answer arguments similar to those here made by petitioner, and these cases show that, apart from "vested property rights" (discussed infra), any rights granted by the corporation laws to creditors and other third persons are taken by them subject to the reserved power of amendment and repeal.

Petitioner suggests (rather than argues) that the provision for directors' liability was not a "law" within the meaning of the California Constitution (Art. XII, Sec. 1, supra) reserving the power of repeal (Pet. pp. 9-10). This argument has not even a shadow of merit. In the first place, petitioner himself, for the purpose of his impairment of contract argument, specifically contends that "a State Constitution is a 'law'" (Pet. p. 19). In the second place, the constitutional provision is the only basis for the liability here asserted against the respondent, and if this provision is not a "law," then there is no basis whatever for petitioner's case. In the third place, the Supreme Court of California, which is, of course, entitled to interpret the State Constitution, decided long ago that the provision for directors' liability is a law (*Winchester v. Howard*, 136 Cal. 432, 439, 64 Pac. 692, 69 Pac. 77) and in the case at bar this same court decided that the provision is a law within the meaning of

the reserved power of repeal (R. pp. 37, 51). In the fourth place, petitioner's argument is made upon an incomplete quotation of the provision of the California Constitution containing the reserved power (Pet. p. 10), and the argument is, we submit, obviously unfounded when the whole provision (quoted supra) is considered.

All through the brief, petitioner makes and repeats the point that the reserved power of repeal cannot be used to destroy "vested rights" (Pet. pp. 6, 7, 9-10, 19, 24-28). This, of course, is elementary, and the Supreme Court of California so held (R. pp. 51-52). Petitioner's argument, however, begs the whole question. A "vested right," as the term is used in the cases, means a right which the constitution protects. For petitioner to call his claim a "vested right" does not prove that it is such a right. The settled rule is, we submit, that an inchoate claim such as that of the petitioner, does not, in view of the reserved power of repeal and under the authorities cited, become a "vested right" until it has been reduced to final judgment.

We respectfully submit that the application for certiorari should be denied.

Dated, San Francisco,
December 17, 1931.

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